

SUBCOMMITTEE NO. 4

Agenda

Joseph Dunn, Chair
Dick Ackerman
Denise Moreno Ducheny



Wednesday, April 28, 2004
1:30 p.m.
Room 3191

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Proposed Consent Calendar

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| 0280 | Commission on Judicial Performance |
| 1705 | Fair Employment and Housing Commission |
| 9860 | Capital Outlay Planning and Studies Funding |

CONTROL SECTIONS:

| | |
|-------|---|
| 4.30 | Lease Revenue Payment Adjustments |
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| 4.80 | State Public Works Board Interim Financing |
| 4.90 | Architectural Revolving Fund Transfer |
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| 6.00 | Project Alterations Limits |
| 8.50 | Federal Funds Receipts |
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| 9.20 | Administrative Costs Associated with the Acquisition of Property |
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| 9.50 | Minor Capital Outlay Projects |
| 11.00 | EDP/Information Technology Reporting Requirements |
| 11.10 | Reporting of Statewide Software License Agreements |
| 11.11 | Privacy of Information in Pay Stubs |
| 11.52 | Transfer of Unencumbered Balance of Various Funds to the General Fund |
| 12.30 | Special Fund for Economic Uncertainties |

| | |
|-------|--|
| 26.00 | Intraschedule Transfers |
| 28.00 | Program Change Notification |
| 35.00 | General Fund Deficit Recovery Payments |
| 35.50 | Estimated General Fund Revenue Per ACA 5 |

Proposed Consent Calendar

Staff Recommendation: No issues have been raised with these budgets. Staff recommends the subcommittee approve all items on the consent calendar.

Vote:

2660 Department of Transportation

The Department of Transportation (Caltrans) constructs, operates and maintains a comprehensive state system of 15,200 miles of highways and freeways and provides intercity passenger rail services under contract with Amtrak. The state highway system comprises approximately nine percent of the total roadway mileage in California but handles approximately 54 percent of the miles traveled. The department also has responsibilities for congestion relief, transportation technology, environmental and worker protection, airport safety, and land use and noise standards. Caltrans' budget is divided into six primary programs: Aeronautics, Highway Transportation, Mass Transportation, Transportation Planning, Administration, and the Equipment Service Center.

The budget proposes total expenditures of \$7.4 billion, a decrease of \$1.1 billion (13.3 percent) from the current-year budget.

Mid-Year Proposals to Aid the General Fund: The Administration and the LAO should update the sub-committee on any new developments and any erosions related to the following Administration mid-year proposals:

- a) Accelerate the receipt of \$800 million in federal reimbursements by utilizing cash management of locally-subvented federal Obligation Authority (OA). With this additional \$800 million in federal reimbursement to the State Highway Account, which was not anticipated in the 2004 STIP Fund Estimate, the Administration proposes the following:
 - Reimburse the General Fund for debt service on current transportation general-obligation bonds (\$406 million).
 - Loan \$200 million to the General Fund for up to 3 years (Proposition 2 loan).
 - Retain \$194 million to support highway project allocations.

- b) Transfer income from the sale of property, rental income, and miscellaneous revenues (“non-Article XIX revenue”) to the General Fund (\$108 million over two years).
- c) Retain gasoline sales tax “spillover” revenue in the General Fund (\$17 million). The sales tax on gasoline and diesel sales is allocated for transportation purposes. A portion of the sales tax on gasoline (and diesel sales) is allocated to the Public Transportation Account (PTA). When gasoline prices are high relative to other non-gasoline sales, the PTA receives the “spillover” sales tax revenues.
- d) Transfer \$189 million from the Traffic Congestion Relief Fund to the General Fund, and repeal the statutory authority for the projects in the Traffic Congestion Relief Program (TCRP). The Administration indicates that the TCR project sponsors will have to secure funding through the State Transportation Improvement Program (STIP), or local funding mechanisms.

Included in the discussion should be the following, which have occurred since the December hearing on mid-year proposals:

- The Administration’s proposal to fully suspend Proposition 42 in 2004-05.
- Finance Letter #1, which requests 16.1 personnel years (two-year limited term) to implement cash management for locally-subvented federal funds.
- The new provisional language proposed by the Administration for the transfer of non-Article XIX funds.
- The survey of TCRP project sponsors concerning close-out costs.

Staff Recommendation: Hold open pending May Revision.

0860 Board of Equalization

The Board of Equalization (BOE) collects state and local sales and use taxes and a variety of business and excise taxes and fees, including those levied on gasoline and diesel fuel, alcoholic beverages and cigarettes. BOE also assesses utility property for local property tax purposes, oversees the administration of the local property tax by county assessors, and serves as the appellate body to hear specified tax appeals. The proposed budget includes \$321.4 million more funding than the current-year level.

| | 2002-03 | 2003-04 | CHANGE FROM 2002-03 | | 2004-05 | CHANGE 2003-04 | FROM |
|------------------|-----------|-----------|------------------------|-------|-----------|-------------------|-------|
| Total Budget | \$316,322 | \$328,256 | \$11,934 | 3.8% | \$326,820 | -\$1,436 | -0.4% |
| Personnel Years* | 3667.8 | 3483.5 | -184.3 | -5.0% | 3461.8 | -21.7 | -0.6% |

(Dollars in 000s)

*Positions adjusted for salary savings and other adjustments

ISSUE #1: Issues Proposed for Consent

The following Finance Letter and Budget Change Proposal have been submitted by the Administration.

| Budget Change Proposals and Finance Letters | | |
|---|--------------------------------------|--|
| TITLE | Positions | Cost (\$s in 000s) |
| Department of Motor Vehicles Fee Increase. It is requested that the BOE's budget be increased by \$687,000 in order to accommodate an increase in the DMV charges for collecting use taxes on behalf of the BOE. The DMV provides these administrative duties to the BOE via an interagency agreement to act as the BOE agent at the time of the DMV registration. | 0 | \$550 General Fund \$137 Reimbursements |
| Annual Water Rights Fee. Ongoing funding and positions are sought to implement and administer the new water rights program under the provisions of Chapter 741, Statutes of 2003 (Senate Budget Committee). This chapter increased the application fees for water rights and assessed an annual fee to be paid and collected by the BOE. The funding pays for the BOE to carry out certain provisions of the Water Code. | 2.2 (2003-04) 3.8 (ongoing) | \$664 reimbursements (2003-04) \$428 Water Rights Fund (2004-05) \$333 Water Rights Fund (ongoing) |

Staff Recommendation. **Approve as budgeted** the Finance Letter and Budget Change Proposal described under Issue #1.

ISSUE #2: Chapter 890, Statutes of 2003, The Cigarette and Tobacco Products Licensing Act of 2003.

Chapter 890, Statutes of 2003, (AB 71) mandated that the BOE administer a statewide program to license businesses that distribute cigarettes and tobacco products (manufacturers, importers, distributors, wholesalers, and retailers). The new program prohibits manufacturers, importers, distributors, and wholesalers from selling cigarettes and tobacco products to an unlicensed distributor, wholesaler, or retailer, and imposes fines and penalties for violation of the law.

Administration Proposal. The Administration's proposal requests positions and funding to be paid for out of the Cigarette and Tobacco Compliance Fund. That fund was established to improve voluntary compliance by reducing smuggling and counterfeiting and receives income through the licensing tobacco businesses.

- \$5,598,000 (Cigarette and Tobacco Products Compliance Fund) and 40.6 personnel years in 2003-04
- \$8,161,000 (Cigarette and Tobacco Products Compliance Fund) and 80.7 personnel years in 2004-05
- \$8,044,000 (Cigarette and Tobacco Products Compliance Fund) and \$80.7 personnel years ongoing

Staff Comment. There has been a decline in both total consumption of taxable cigarettes and per capita consumption of taxable cigarettes over the last ten years. During this period, the cigarette tax has increased from 10 cents to 87 cents per pack. In addition, there are new statewide restrictions on smoking in public buildings. These restrictions and the increased price of cigarettes have resulted in some decline in consumption. Some of this decline, however, is due to an increase in the consumption of untaxed cigarettes. Major areas of cigarette tax evasion include stamp counterfeiting, smuggling across state or international borders, Internet purchases, and unstamped products.

Staff Recommendation.

1. **Request the BOE report to the Subcommittee on General Fund revenues to be gained** through increased voluntary compliance resulting from this law in 2003-04 (revenues to date), 2004-05, and 2005-06 and beyond.
2. **Hold open.** Based on the possibility of revised General Fund revenue estimates, staff recommends the Subcommittee leave this issue open for reconsideration after the May Revision has been released.

ISSUE #3: Allocation of Reductions Pursuant to Control Section 4.10

Board of Equalization Control Section 4.10 Plan. The BOE reports that approximately \$35.5 million (\$27 million General Fund) will be lost due to the implementation of the Control Section 4.10 reduction plan. In deciding where to reduce positions BOE used the following priorities:

- (1) Prevent layoffs
- (2) Minimize revenue losses to the state and local governments
- (3) Eliminate vacant positions.

In implementing their plan, the BOE lost 141 positions and over \$16 million in funding, with \$3.8 million of that reduction taken from operating expenses and equipment (OE&E) and the remainder (\$12.2 million) from personal services.

LAO Recommendation. The LAO estimates that approximately \$20 million of the General Fund revenues lost due to 4.10 reductions could be recaptured if the BOE revised their Control Section 4.10 plan. The BOE plan includes 91 positions that will have a negative impact on the collection of revenues.

Staff Comment. The Subcommittee should note the value that BOE has placed on preventing layoffs, relative to minimizing General Fund revenue losses. Based on the LAO's assessment that 91 revenue producing positions are being eliminated and \$20 million could be reclaimed, each of the 91 positions represents an average of approximately \$220,000 in lost revenues to the state.

Staff Recommendation.

- (1) **Hold open** for reconsideration after the May Revision has been released and the extent of the General Fund shortfall is updated.
- (2) **Request the BOE report to the Subcommittee** on the LAO's estimates of lost revenue due to the implementation of their Control Section 4.10 plan.

ISSUE #4: Board Staff Reduction

LAO Recommendation. The LAO has provided a recommendation that the Legislature reduce the budget authority for staff support positions for Board members of the BOE and reset their budget authority to the 2002-03 level. This reduction would result in savings of \$700,000 General Fund and \$300,000 special fund reimbursements, as well as a reduction of 14 positions. The LAO asserts that tasks for the Board have not changed appreciably since 2002-03 and that it is reasonable that the Board itself absorb losses to staff support.

Staff Comment. In light of the Control Section 4.10 revenue losses, the LAO proposal may constitute a practical assignment of the staff reduction that will not hinder revenue collections.

Staff Recommendation. **Hold open** until after the May Revision has released and the extent of the General Fund shortfall is updated.

ISSUE #5: Cigarette and Tobacco Distributor Twice-Monthly Payment and Reporting pursuant to Chapter 867, Statutes of 2003 (AB 1666)

Administration's Proposal. The Administration requests the BOE's budget be augmented by \$53,000 and .5 position on a limited-term basis through December 31, 2006. This funding and position are sought to implement the provisions of Chapter 867, Statutes of 2003 (AB 1666), which allows cigarette and tobacco product distributors to elect to file excise tax returns either on a monthly or twice-monthly basis (a potential tax benefit for tobacco distributors). This proposal also provides funding for the associated Bank of America contract to process additional payments and reconcile accounts.

Staff Comment. Staff notes that this proposal could potentially result in additional revenues for the state. Chapter 867, Statutes of 2003, directs the LAO to report back by January 1, 2006, on additional revenues generated by increasing the periodicity of payments.

Staff Recommendation. **Hold open** for reconsideration after the May Revision has been released and the extent of the General Fund shortfall is updated.

ISSUE #6: Special Taxing Districts—Reimbursement Level

A primary responsibility of the BOE is to administer the state's sales and use tax (SUT). BOE administers the SUT on behalf of local governments and special districts. These agencies must then reimburse the BOE for collection and allocation costs.

Chapter 890, Statutes of 1998 (Sweeney) required the BOE in certain circumstances to cap the reimbursements it receives from special taxing districts, in order to make tax assessments more financially feasible for these districts.

LAO Recommendation. The LAO recommends the Legislature make the special taxing districts self-supporting by ending the caps on reimbursements it may receive for administrative costs. This action is estimated to reduce the General Fund appropriation of this item by \$1.3 million annually. Reimbursements would be increased by an equivalent amount.

Staff Recommendation.

- (1) **Request the BOE report to the Subcommittee** on the findings of their Special Taxing Jurisdiction model and any other concerns with the LAO proposal.
- (2) **Reduce the General Fund appropriation item (0860-001-0001) by \$1.3 million and increase reimbursements by an equal amount.**

VOTE:

ISSUE #7: Field Office Consolidations

The BOE currently maintains 27 field offices throughout the state and four nationwide (Houston, Chicago, New York, and the Sacramento "out of state" office). These offices provide technical and general information support to taxpayers.

LAO Issue. The LAO questions the need for 31 field offices and points out that a like agency (the FTB) is undertaking a comprehensive review of their 16 field offices to determine which facilities can be closed. (Some of their 16 are actually co-located with BOE offices.) The LAO asserts that technology efficiencies (e.g. Internet, telecommunications) could reduce the need for face-to-face interaction and allow field offices to be closed, saving the state millions of dollars annually.

LAO Recommendation. The LAO recommends the following supplemental report language be adopted by the Legislature to initiate a review of the BOE's facilities needs.

The Board of Equalization (BOE) shall provide to the Chair of the Joint Legislative Budget Committee and the chairs of the fiscal committees of the Legislature by December 1, 2004, a report containing the following information: (1) unit costs of providing taxpayer services and audit and collection activities at the BOE's 27 field offices; (2) net annual budgetary benefits of consolidating or closing four BOE field offices (one in each BOE district); (3) estimated impact on all BOE-collected tax revenues from field office consolidations or closures identified in (2) above;

(4) net annual benefits of reducing or eliminating an out-of-state office. Data provided shall include one-time and ongoing budgetary and revenue impacts.

Staff Comment. Notwithstanding the short-term costs associated with breaking leases, it is unclear that technology efficiencies (e.g. Internet, telecommunications) won't overcome those temporary expenses. The proposed LAO supplemental report language is a vehicle to address this uncertainty.

Staff notes that by closing the field office in Torrance (independent of an external recommendation to do so), the BOE demonstrated a commitment to controlling facilities costs. The BOE estimates that the 2004-05 savings for this closure to be \$296,000 General Fund and \$74,000 in reimbursements. However, at the April 27, 2004, Assembly Subcommittee #4 hearing, the BOE suggested that the savings were "half a million."

Staff Recommendations:

- (1) Adopt the LAO's proposed supplemental report language.**
- (2) Request the BOE report on the actual amount of General Fund and other savings generated by the closure of the Torrance office.**
- (3) Reduce the BOE's General Fund appropriation by the amount identified in (2) to reflect the savings generated by the closure of the Torrance field office.**

VOTE:

ISSUE #8: Out of State Field Offices

The BOE operates three out of state offices, Chicago, New York, Houston, and one office in Sacramento for out of state services.

Staff Comment. In light of the state's General Fund shortfall and the recent precedent for closure of out of state offices (e.g. the Technology, Trade, and Commerce offices), the need for out of state offices is questionable. Furthermore, advances in information technology suggest that the duties performed by the BOE may be accomplished without face-to-face interaction in other parts of the country.

Staff Recommendation:

- 1. Request the BOE report to the Subcommittee** on the unique benefits provided by each of the out of state offices and identify the revenue impacts to basing all out of state activity from the Sacramento "out of state" office.
- 2. Staff recommends the following supplemental report language be adopted** by the Legislature to initiate a review of the BOE's out of state facilities needs. If adopted, provision (4) of the supplemental report language under Issue #8 ("Field Office Consolidations") should be removed.

The Board of Equalization (BOE) shall provide to the Chair of the Joint Legislative Budget Committee and the chairs of the fiscal committees of the Legislature by December 1, 2004, a report containing the following information: (1) unit costs of providing taxpayer services and audit and collection activities at the BOE's out of state offices; (2) net annual budgetary benefits of closing the four BOE out of state offices; (3) estimated impact on all BOE-collected tax revenues from out of state office closures identified in (2) above; (4) net annual benefits of reducing or eliminating all out-of-state offices. Data provided shall include one-time and ongoing budgetary and revenue impacts.

VOTE:

ISSUE #9: INFORMATIONAL ISSUE

Senate Bill 17 (Escutia), Property Taxation: Change in Property Ownership

Current property tax law is framed by Proposition 13, the landmark tax reform measure of 1978. Among other effects, Proposition 13 froze property tax levels at the level of that year and allowed property value reassessments only when properties are sold.

Among owners of commercial properties, reassessments are sometimes subject to manipulation. For example, the commercial interest may simply not report a sale and thereby escape reassessment.

Senate Bill 17 is an attempt to curb the practice of reassessment evasion by making the following changes to law:

- (1) Requiring the Franchise Tax Board (FTB) to furnish the BOE with the name and address of any entity that does not respond to a question concerning change in ownership on partnership, bank, and corporate returns.
- (2) Requiring publicly traded companies to file annual real property statements with the BOE and impose penalties for failure to file the statement.
- (3) Modifying and increasing the penalty assessed when a legal entity does not file a change in ownership statement with the BOE after a change in ownership.
- (4) Making various legislative findings and declarations related to change in ownership of nonresidential and commercial properties.

Staff Comment.

If enacted, this bill could annually generate hundreds of millions in new General Fund revenue by reducing the incidence evasion of property tax reassessments. In curbing evasion by certain commercial property owners, the property tax will be more equitably borne. Additionally, penalty revenues would also provide some General Fund relief.

Staff Recommendation. Request the BOE report to the Subcommittee on revenue impacts, including increased property tax revenues and penalties associated with this bill, and other policy implications related to this bill.

1100 California Science Center

The California Science Center is an educational, scientific and technological center administered by a nine-member board of directors appointed by the Governor. It is located in Exposition Park, a 160-acre tract just south of the central part of Los Angeles, which is owned by the State. The Science Center presents a series of exhibits and conducts associated educational programs focusing on scientific and technological developments of the State. The California African American Museum is housed in a building adjacent to the Science Center and receives state funding through the Science Center budget.

The Science Center budget is proposed to increase from \$19.9 million in the current year to \$20.1 million in the budget year – an increase of \$132,000. The General Fund support in the current year is \$12.8 million and is proposed at \$14.2 million in the budget year – an increase of \$1.4 million.

Issues Proposed for Consent

1. **Operating Budget for the New Parking Facility (BCP #2).** The Administration requests \$260,000 in special funds for the operation of the new California Science Center and California African American Museum Parking Facility. The parking facility would also be used for event parking for the Los Angeles Sports Arena and the Los Angeles Memorial Coliseum.

Staff Comment: The Science Center estimates parking revenue from this new facility will exceed operation costs. No General Fund savings would result from delaying the opening of this new facility.

2. **Technical Correct to California African American Museum (CAAM) Reimbursements (April FL).** The Administration requests a \$1 million reduction in reimbursements to correctly reflect the completed expenditure of bond funds provided to the CAAM in the Budget Act of 2000.

Staff Comment: No concerns have been raised with this technical correction.

3. **Restoration of 3.0 Positions for the California African American Museum (CAAM) – No New Funding is Requested. (FL # 1).** The Administration requests the restoration of 3 positions eliminated by Government Code 12439 (vacant for more than 6 months). These positions were deemed critical by the Administration and not included in the Control Section 4.10 reductions. Funding was retained in the budget for these 3 positions and therefore no funding augmentation is necessary.

Staff Comment: According to the Administration, these positions were vacant during a period when the museum was under renovation and therefore the vacancies were manageable. The CAAM re-opened in March 2003 and the Museum is now requesting restoration of the positions.

Staff Recommendation: Approve the Administration's requests. No issues have been raised with these consent items.

Vote:

Discussion Issues

- 1. Staff and Operational Costs for the New Science Center School and the new Center for Science Learning (BCP #1).** The Administration requests 23 positions (21.9 personnel years) and \$2.424 million, of which \$1.443 million is state General Fund and \$981,000 is reimbursements from the Los Angeles Unified School District (LAUSD), for operational costs for the new Science Center School and the new Center for Science Learning. The Science Center School will operate as a neighborhood charter school and serve 720 K-5 students. The Center for Science Learning will serve the 720 students and faculty, and be incorporated into ongoing Science Center education programs. The request includes 16 facilities operations staff (i.e. Janitors and Stationary Engineers) and 7 program related staff (i.e. Exhibit Designer-Installer, Office Technician, Education Administrator). The LAUSD would fund approximately half of the facility operations cost, and none of the Learning Center program costs.

LAO Option: Delay the opening of the Center for Science Learning for General Fund savings of \$1.4 million. The LAO indicates the charter school could be opened without General Fund support, since it is funded by the Los Angeles Unified School District. The option is to delay opening the Center for Science Learning, which would eliminate the Center for Science Learning programming for the K-5 charter school and other educational groups that would use the facility. The charter school would still have access to the nearby California Science Center.

Staff Comment: The Science Center disputes the LAO finding that the Science Center School could be opened, but the opening of the Center for Science Learning deferred, to generate General Fund savings of \$1.4 million. Since the Learning Center and the School are located in the same building and share common areas and utilities, the Science Center indicates some savings would occur with the LAO option, but not the full amount suggested. A staff analysis of the BCP indicates that savings of at least \$900,000 General Fund should be feasible if the Center for Science Learning and its associated programs were deferred until 2005-06.

Staff Recommendation: Discuss the LAO Recommendation below prior to taking an action on this issue. The Staff Recommendation for Issue #1 and Issue #2 are combined below in the Issue #2 Recommendation.

- 2. Phase Out of General Fund Support for Science Center Operations (LAO Recommendation).** In the current year, the Science Center receives \$8.7 million in General Fund support for operations, and \$2.7 million in General Fund for the payment of lease revenue bonds. An additional \$1.4 million is requested in 2004-05 for the Science Learning Center. The California African American Museum receives General Fund of \$1.9 million. Total General Fund support is proposed at \$14.2

million in 2004-05. The Science Center does not currently charge an entrance fee, but operates associated programs that do charge fees such as the IMAX theater and private events and parties.

LAO Recommendation: Phase out General Fund support for operational costs (a \$5.0 million reduction in 2004-05 and an additional \$3.1 million reduction in 2005-06) and backfill this funding with new admission fees, increases in other charges, and Science Center Foundation revenue. Continue General Fund support for lease-revenue bond payments and for the California African American Museum.

Staff Comment on the LAO Recommendation: The Science Center has performed an analysis that suggests charging admission fees would significantly reduce attendance and the ethnic diversity of the attendees, and would not generate sufficient revenue to replace lost General Fund revenue. A staff review of the information suggests that it may be difficult to backfill \$8.1 million in General Fund support with entrance fees; however, opportunities do exist to generate additional fee-generated funding and to shift some activities supported by the General Fund to the Science Center Foundation.

Staff Alternative to the LAO Recommendation: If the subcommittee does not wish to phase out General Fund support for the Science Center operations, an alternative would be to hold General Fund at the current-year level and deny the request for the \$1.4 million General Fund augmentation (Issue #1 above). The Science Center would have then have the option to increase fees to cover the new costs, to cut costs in other areas (i.e. reduce the funding for new exhibits or reduce hours of operations, etc.), or appeal to donors to cover the cost of new operations.

Staff Recommendation on Issues #1 and #2: Deny the funding augmentation requested in Issue #1, but approve reimbursements from the Los Angeles Unified School District. This would reject General Fund support in 2004-05 for new or expanded Science Center activities. Keep the Science Center budget open and direct staff to work with the Science Center to determine if any funding shift between operating expenses and equipment (OE&E) and personal services is desirable. Note, new positions could be added for the Center for Science Learning without General Fund cost, if OE&E is reduced by the same amount. These OE&E costs would then have to be funded from increased fees or Foundation support.

Vote:

1700 Department of Fair Employment and Housing

The Department of Fair Employment and Housing (DFEH) has the mission of protecting the people of California from unlawful discrimination in employment, housing and public accommodations, and from the perpetration of acts of hate violence.

The DFEH budget is proposed to decrease from \$19.9 million in the current year to \$18.7 million in the budget year – a decrease of \$1.2 million. The General Fund support in the current year is \$13.5 million and is proposed at \$13.5 million in the budget year.

Issues Proposed for Consent

- 1. Federal Fund Augmentation of \$1 Million to Match Receipts and Resolve an Operating Expense Shortfall (BCP #1).** The Administration requests an augmentation of \$1 million in federal funds to align the department's budget to its annual federal receipts, and to partially resolve a structural shortfall within the department budgets. The Administration indicates that an operating expenses shortfall has existed since 1998-99 due to unfunded rent increases and other costs. The department has used using salary savings and the Section 28.00 process (to bring in additional federal funds) to meet its fixed costs.

Staff Comment: A December 11, 2003, Section 28.00 letter was submitted and by DFEH that requested \$1,000,000 in additional federal funds expenditure authority. The Section 28.00 letter indicated that this was a structural issue that would be addressed in the Governor's Budget. The DFEH indicates that it has already significantly reduced its communications, printing, travel, training and general expenses. No General Fund augmentation is included in this request.

- 2. Postage and Other Savings from Chapter 447, Statutes of 2003 (BCP # 3).** The Administration requests to reduce the DFEH budget by \$75,000 (\$38,000 in the current year) to reflect savings that result from Chapter 447, Statutes of 2003 (AB 1536). Chapter 447 allows DFEH to serve only those complaints that are filed for investigation by certified mail and therefore saves postage cost. The legislation also provides that where a person claiming to be aggrieved by an unlawful practice is represented by private counsel, private counsel, and not the department, would serve the complaint.

Staff Comment: No issues have been raised with this request.

Staff Recommendation on Consent Issues: Approve the Administration's requests.

Vote:

Issues for Discussion

- 1. Handle Complaints Through Mediation (LAO Option).** The 2000-01 Budget Act included \$1 million in funding for a pilot mediation program. Under the program, parties using the program agreed to mediate the complaints instead of having the department investigate complaints. The LAO reports that an independent evaluation found that participants were satisfied with the program and that cases that went through mediation cost the state \$500 less than the average case.

LAO Option: Direct 2,000 cases (20 percent of total cases) to mediation for a General Fund savings of \$1 million.

Staff Comment: The department indicates that the mediation process resulted in no net savings. While cases settled through mediation did result in an average savings of \$500, cases not settled through mediation then went to investigation – with mediation only adding costs to those cases.

Staff Recommendation: Withhold action on the LAO option at this time since the DFEH indicates no savings would result.

Vote:

2. **Return Joint Jurisdiction Cases to the Federal Government (LAO Option).** By agreement with the federal government, the department investigates complaints on behalf of the Equal Employment Opportunities Commission (EEOC) and the Department of Housing and Urban Development (HUD) when there is joint jurisdiction between federal and state law (approximately 70 percent of department cases according to the LAO). The EEOC and HUD reimburse the department for part of the investigation expenses (about one-third for most cases, again according to the LAO). The General Fund covers the remaining costs.

LAO Option: Return to the EEOC and HUD the joint-jurisdiction cases and reduce DFEH staffing and funding for a General Fund savings of \$8 million.

Staff Comment: The DFEH indicates that many joint-jurisdictional cases involve state laws that are broader than federal laws (such as in the area of disabilities) – in which case portions of the state law would not be enforced.

Staff Recommendation: Withhold action on this LAO's option at this time. The subcommittee may wish to consider revisiting this item at a later date, or adding this proposal to a potential savings list.

Vote:

1730 Franchise Tax Board

The Franchise Tax Board (FTB) is one of the state's two major tax collection agencies and is primarily responsible for the collection of personal income and corporate taxes. The FTB also administers the Senior Homeowners and Renters' Assistance program, the Political Reform Audit Program, and several non-tax-related programs, among those the collection of delinquent child support payments. The FTB is governed by a three-member board, consisting of the Director of Finance, the Chair of the Board of Equalization, and the State Controller. An executive officer, appointed by the board, administers the daily operations and functions of FTB. FTB is funded at \$560 million in the budget year, of which \$441 million is General Fund.

| | | | | | | |
|--|---------|---------|-------------|---------|--------|------|
| | 2002-03 | 2003-04 | CHANGE FROM | 2004-05 | CHANGE | FROM |
|--|---------|---------|-------------|---------|--------|------|

| | | | | | | | |
|------------------|-----------|-----------|----------|-------|-----------|----------|-------|
| | | | 2002-03 | | | 2003-04 | |
| Total Budget | \$441,344 | \$532,643 | \$91,299 | 20.7% | \$560,536 | \$27,893 | 5.2% |
| Personnel Years* | 5745.6 | 5215.2 | -530.4 | -9.2% | 5075.0 | -140.2 | -2.7% |

(Dollars in 000s)

*Positions adjusted for salary savings and other adjustments

ISSUE #1: Issues Proposed for Consent

The following Finance Letters and Budget Change Proposals have been provided by the Administration.

| Budget Change Proposals and Finance Letters | | |
|---|-----------|--|
| TITLE | Positions | Cost (\$s in 000s) |
| California Child Support Automation System (CCSAS). This ongoing project will facilitate child support payments from delinquent parents. Budget year funding is needed to make payments for procurement activities. Failure to implement CCSAS results in a significant loss of federal TANF funding. | 0 | \$33,806: \$12,493 GF and \$21,313 reimbursements (one year) |
| California Missions Foundation Fund. Funding is sought for administrative costs for processing contributions to the California Missions Foundation Fund, a "check in the box" option on state tax returns. Chapter 460, Statutes of 2003 (Speier) established this donation option through 2008. | 0 | \$1,000 California Missions Foundation Fund |
| Voter Registration Card. The FTB seeks reimbursement for printing costs associated with adding a voter registration card to all 2003 personal income tax booklets. Approximately 3.5 million books are mailed annually. Chapter 412, Statutes of 2003 (Poochigian) established this requirement. | 0 | \$236 GF |
| Phase III Occupancy Costs. Funding for ongoing maintenance and operations for the FTB's new State office building complex (known as Phase III), consisting of a new office, central plant, and warehouse buildings. This project was approved by Chapter 328, Statutes of 1998 (Vargas, Koretz, and Lieber). | 0 | \$6,467,000: \$6,046 GF \$259 Reimbursements \$27 Motor Vehicle Account \$50 Motor Vehicle License Fee Account \$85 Court Collection Account |
| Central Processing Unit Augmentation. Industry standards recommend 90 percent capacity for the CPU for tax processing, which allows for a 10 percent buffer. Based on projected growth, the system will be at 101 percent capacity in 2004-05. The feasibility study report for this project has been approved by Finance. | 0 | \$1,013 GF |

| | | |
|--|---|----------|
| Resident Real Estate Withholding. This proposal seeks to provide funding for 11.5 positions for the resident real estate withholding program, which was established last year. FTB has identified the pertinent workload and determined that future revenue collections of \$157 million will be at risk if these positions are not approved. | 0 | \$575 GF |
|--|---|----------|

Staff Recommendation. Approve as budgeted the Finance Letters and Budget Change Proposals described under Issue #1.

ISSUE #2: Political Reform Audit Fee.

The Political Reform Audit Program was enacted in the wake of the Watergate scandal and has been a responsibility of the FTB since 1975. This program determines the accuracy of political statement reports filed the Secretary of State and conducts randomly selected field audits of political committees.

Administration Proposal. The Administration requests to change the funding source for the Political Reform Audit (PRA) Program from the General Fund to the new Political Reform Audit Fee Fund. As proposed, the PRA Program will be funded by \$1,442,000 in fees collected from candidates for elected political offices at the state level, as well as lobbyists, lobbying firms, lobbying employers, and certain political committees. The proposed fees will be used to defray the cost of the mandated audits.

Trailer Bill. The trailer bill proposed to implement this proposal would impose a fee on certain candidates filing for elected public offices, lobbyists, lobbying firms, lobbyist employers, and certain committees for deposit in the newly established fund.

The language requires the FTB to notify the Department of Finance biannually of the existing fee amount, the current fiscal year costs for the audit program, projected costs for the next two fiscal years, and the recommended fee amount for the next two years. The Director of Finance is directed to report on the amount of any fee increase no later than June 30, 2004 and biannually thereafter. This section is intended to ensure that the fee matches program costs.

Staff Comment. The new fee will be set to generate \$1.36 million to pay for the audit costs of the FTB. If this fee is not adopted, Item 8640 (Political Reform Act of 1974) must be augmented by \$1.36 million (GF). While not yet implemented into the trailer bill, staff has been told that fees will be set at the following levels.

| ASSESSED PARTY | VOLUME | FEE | TOTAL REVENUE |
|--|---------------|------------|----------------------|
| Lobbyists (individuals and firms) | 1,000 | \$757 | \$757,000 |
| Ballot measure committees | 54 | \$757 | \$40,878 |
| Political party, PAC, and other general purpose committees | 500 | \$757 | \$378,500 |
| State candidate committees | 325 | \$757 | \$246,025 |

| | |
|--------------------------|--------------------|
| TOTAL FEE REVENUE | \$1,422,403 |
|--------------------------|--------------------|

A number of concerns have emerged with regards to this proposal. First, this proposal may be subject to litigation. The FPPC has identified the potential for a lawsuit based on the state forcing disclosure by committees and individuals and then assessing fees from those who are to be audited. It is also anticipated that lobbying organizations will file suit based on infringement of their rights. Second, the litigation costs may be substantial, based on the possible suits to be filed.

Staff Recommendation. Hold open and request testimony on:

1. Issues related to potential litigation and potential litigation costs.
2. The rationale for the specified committees and state-level offices designated for a fee.
3. (From the FTB) Reasons why the fee is set to fund the FTB portion only, and not the related activities of the FPPC and Secretary of State

ISSUE #3: Substandard Housing Mandate (Chapter 238, Statutes of 1973)

Revenue and Taxation Code Sections 17274 and 24436.5 provide that if a taxpayer derived rental income from substandard housing, no deduction for interest, taxes, depreciation, or amortization paid in conjunction with substandard housing is allowed.

The mandate is created by local housing agencies having to report these taxpayers to the counties, who in turn must report them to the state. The FTB has stated that in the last three years this mandate has been suspended, they have not encountered difficulty in retrieving the information necessary from local agencies to carry out this activity.

Administration Proposal: Suspend the Substandard Housing Mandate.

LAO Proposal: Repeal the Substandard Housing Mandate.

Staff Comment. Most recently, this mandate was suspended in 2001-02, 2002-03, and is suspended in the current year.

Staff Recommendation.

1. **Hold open** pending a recommendation from the policy committee who reviews this mandate.

ISSUE #4: Fees for Franchise Tax Board Services

The FTB provides a variety of services to individuals and businesses to facilitate the collection of personal income and corporations taxes. Some of these services are distinct from normal tax administration and processing activities and constitute a commitment of state resources for the benefit of individual taxpayers.

LAO Recommendation: The LAO recommends that the Legislature adopt language that would allow the FTB charge fees for the services identified below and generate a General Fund savings of approximately \$3.9 million ongoing. These fee proposals are not inconsistent with the fees already charged for similar services by the Internal Revenue Service. Specifically, the LAO recommends the following services be assessed fees at the indicated rates.

| SERVICE | PROJECTED VOLUME | PROPOSED FEE | PROJECTED REVENUE |
|--|------------------|--------------|-------------------|
| Installment Agreements. These are agreements that allow certain taxpayers to schedule periodic partial payments on a balance due of under \$10,000 that can be fully paid within 36 months. | 117,600 | \$15 | \$1,764,000 |
| Tax Practitioner Hotline. This service provides technical support to professional tax practitioners. The FTB reports that an annual fee would be the least obtrusive method to accounting professionals. The fee would be set to pay for program costs only (approximately \$750,000/year). | 200,000 | (variable) | \$750,000 |
| Refund Stop Payment. The purpose of this processing activity is to prevent a refund warrant to be cashed by an unauthorized individual. | 52,345 | \$10 | \$523,450 |
| Transcript Preparation or Tax Computation. These activities require the preparation of a document or report showing annual activity on a taxpayer's account including: filings, tax amounts, penalty amounts, interest amounts, payments, assessments, credits, and refunds. | 47,292 | \$10 | \$516,420 |
| Lien Release or Subordination. This service requires the review and analysis of extensive documentation in order to determine whether the removal or subordination of a state tax lien from a specific piece of property is appropriate, prudent, and justified. | 500 | \$145 | \$72,500 |
| Rush Services. These services provide 24-hour "turn-around" for various actions including corporation reviver (brings a corporation out of suspension), escrow demand (used to process lien releases), entity exemption (for tax-exempt corporation status), and estate income tax certificate (certification of taxes paid). | 20,980 | \$10 - \$75 | \$257,500 |

| | |
|--|--------------------|
| TOTAL PROJECTED REVENUE FROM ALL NEW FEES | \$3,883,870 |
|--|--------------------|

Staff Recommendation. Hold open. Staff recommends the Subcommittee leave this issue open for reconsideration until after the May Revision has released and the extent of the General Fund shortfall is updated.

ISSUE #5: Revenue Acceleration Program.

LAO Issue. The Revenue Acceleration Program was established in 2002-03 to allow FTB to waive the payment of penalties and interest for taxpayers owing balances, in exchange for their immediate payment of unpaid taxes. The program was targeted to taxpayers who had not responded to notices, liens, levies, and telephone contact for at least two years. For the year that the RAP operated (between October 2002 and October 2003), the program is estimated to have generated \$32 million. If this program were to be extended, the FTB has preliminarily estimated that extending the program will net approximately \$20 million.

LAO Recommendation. Request the FTB report at hearings regarding final cost and revenue results of the initial RAP as well as provide estimate costs and revenue to the state resulting from extending the RAP for an additional year.

Staff Comment. This proposal may have some overlap with issue #9 (Tax Amnesty), with regards to revenue scoring. The overlap will be described under that issue.

Staff Recommendation. Request the FTB report to the Subcommittee regarding
(a) final cost and revenue results of the initial RAP and provide an estimate of costs and

(b) revenues to the state if the RAP were extended for an additional year.

(c) the overlap of issues related to this proposal.

ISSUE #6: Independent Contractors and Self-Employed Individuals – Unreported Income

LAO Issue. The LAO has explored a fiscal problem wherein underreported income, specifically by self-employed individuals and independent contractors, costs the state potentially hundreds of millions of dollars. One reason this problem occurs is because payments to independent contractors do not require the withholding of taxes. Consequently, if the independent contractor does not report the income, it remains untaxed.

LAO Recommendation. In an effort to close the “tax gap” (the amount of taxed owed versus the amount of tax actually paid), the LAO proposes additional filing and enforcement measures for independent contractors and self-employed individuals. The

LAO recommends the FTB report to the Legislature on a number of corrective proposals.

Staff Recommendation. Request the FTB report to the Subcommittee on

- a. The viability of **businesses** withholding taxes on certain non-wage workers as a means to reduce the tax burden borne by compliant taxpayers. A withholding rate of 3.5 percent to 5 percent is proposed.
- b. The potential costs and estimated revenues of implementing that proposal.

ISSUE #7. District Office Service Reductions

LAO Issue. The FTB operates 16 field offices throughout the state in order to serve the public. These offices provide face to face consultations, as well as call centers, Internet, and voice response-based systems. The public access counters at the field offices are the most expensive option available for taxpayer assistance. The FTB has recently taken action to close public access counters at all district offices except for six offices. In the wake of these service reductions, the need for the field offices is in question.

LAO Recommendation. In light of the closure of public access windows and other activities at some field offices, the FTB should report at budget hearings on the district office restructuring proposals, including budget changes and state revenue impacts.

Staff Recommendation. Request the FTB report to the Subcommittee on the district office restructuring proposals, including budget changes and state revenue impacts.

ISSUE #8: Personal Income Tax (PIT) Nonfiler Program.

The FTB requests 29.5 positions and \$1.8 million General Fund to perform manual review, write correspondence, and answer calls on PIT nonfiler accounts. This program identifies and gains compliance from individuals who are filing returns by using a variety of manual and automated processes. Each year when potential nonfilers are identified, there are over 268,000 accounts placed in review status. This will enable the FTB to expand this activity by 134,000, up to 268,000.

Staff Comment. This program is predicted to result in new General Fund revenues for the state. Revenue estimates for this program are \$12.3 million in 2004-05, increasing to \$63 million by 2007-08. Based on those estimates, the positions are expected to pay for their expense several times over.

Staff Recommendation.

- (1) **Request the FTB report to the Subcommittee on the basis for the General Fund revenue estimates.**

(2) Approve the Personal Income Tax Nonfiler Program proposal as budgeted.

VOTE:

ISSUE #9: Tax Amnesty

Tax amnesty programs are designed to encourage payment from people and businesses that have not paid past tax debts. By establishing a period wherein penalties will not be assessed if the payments are made by a certain date, the state expects to receive revenues that might otherwise not have been collected.

The fiscal benefits of amnesty programs can be significant. Illinois and New York have had very successful amnesty programs in recent years, generating over \$500 million each. Besides the fiscal benefits to the state, tax amnesty programs are an excellent means to reduce the tax burden borne by businesses and individuals who do pay their fair share of taxes.

California's latest tax amnesty program, called the Voluntary Compliance Initiative (VCI) was estimated to generate approximately \$90 million in 2003-04. **As of April 26, 2004, the VCI had netted over \$1 billion.** That number is expected to increase further as final receipts are calculated. The breakdown was as follows:

- Approximately \$600 million has been paid in Personal Income Tax (568 taxpayers), an average of \$1 million per personal income tax payment.
- Approximately \$400 million has been paid in Corporation Tax (296 taxpayers), an average of \$1.35 million per corporate tax payment.
- Of all 864 taxpayers partaking in the VCI, the average payment was \$1,157,407.

AB 2203. Assembly Member Chu has called for a new broad-based amnesty period for personal income tax and corporation tax to be applied between February 1, 2005 and March 31, 2005 (or any other two-month period in 2004-05). This bill has gone to the Appropriations Committee.

According to the FTB analysis of the bill, the gross amount of revenue from the amnesty bill is \$595 million, \$50 million of which is attributable to penalty revenues established in the bill. Actual new revenue generated is \$55 million. The remaining \$490 million is money that would have been received even absent the amnesty and represents a revenue acceleration.

The \$490 million that would have been received notwithstanding AB 2203 would have penalties associated with it as well. The amnesty program waives those penalties—a revenue reduction to the state.

Staff Recommendation: Request the FTB report to the Subcommittee on the following issues:

1. The reasons for the enormous underestimation of revenues from the VCI and how this miscalculation affects other revenue estimates that have been built into the Governor's Budget and proposed changes to the Governor's Budget.
2. The existence of non-taxpayers (other than the 864 who complied this year) who may comply during a later amnesty period or to a different type of compliance incentive.
3. AB 2203, including the potential revenue and compliance issues.
4. The General Fund revenue "overlap" from the Revenue Acceleration Program proposal (issue #4) relative to the amnesty proposed in AB 2203.

ISSUE #10: Abusive Tax Shelters

Recent data collected by the Internal Revenue Service and interpreted by the General Accounting Office (GAO) suggests that ATS' are proliferating nationwide. In the nine-month period between January 2003 and September 2003, the GAO estimated that the number of ATS transactions increased by 42 percent. The associated loss of revenue to the country over that period rose from \$74 billion to \$85 billion.

In California, the Multistate Tax Commission (MTC) found in a 2001 study that the state's annual revenue losses from ATSS were approximately \$1.3 billion. Today, the FTB estimates that **losses to the state due to ATS activity range from \$600 million to \$1 billion annually.**

According to the LAO, abusive tax shelters (ATSS) usually have the following characteristics:

- They are promoted with the promise of tax benefits
- They have predictable tax losses or tax consequences
- They involve a literal reading of a tax statute inconsistent with its underlying intent.

The FTB and Internal Revenue Service identify ATSS as having no true economic purpose and existing solely for the reason of tax avoidance.

LAO Recommendation. The LAO recommends the FTB report on:

- a. the current status of its ATS enforcement activities,
- b. the need for and potential effectiveness of the following activities
 - Restricting the issuance of tax insurance policies available to investors in ATSS.
 - Expanding California's False Claims Act (which provides for penalties for making a false claim against the state) to include claims, records, or statements made under the Revenue and Taxation Code.
- c. the value and benefits of an integrated plan for ATS enforcement.

2. Also, the LAO recommends the FTB expand its existing annual *Supplemental Report on FTB Audits and Collections Activities* to include a section that specifically addresses the status of ATS enforcement activities

Staff Recommendation.

1. **Request the FTB report to the Subcommittee on:**
 - a. The current status of its ATS enforcement activities
 - b. The need for and potential effectiveness of the following activities
 - Restricting the issuance of tax insurance policies available to investors in ATSS.
 - Expanding California's False Claims Act (which provides for penalties for making a false claim against the state) to include claims, records, or statements made under the Revenue and Taxation Code.
 - c. The benefits of an integrated plan for ATS enforcement
 - d. The steps necessary to implement the recommended elements of (a), (b), and (c).
2. Adopt the LAO proposal and direct the FTB to expand its existing annual *Supplemental Report on FTB Audits and Collections Activities* to include a section that specifically addresses the status of ATS enforcement activities

VOTE (on recommendation 2.)

ISSUE #11: Abusive Tax Shelters Consultant Services

The Administration has requested that FTB's General Fund appropriation be increased by \$400,000 to provide funding for contracts with tax shelter experts whose expertise will assist the FTB in identifying and sustaining assessments for abusive tax shelters and in understanding overseas financial markets. FTB staff does not yet have sufficient experience in this area. The FTB indicates it needs assistance and training to identify and analyze complex abusive tax shelters. The Internal Revenue Service has also found it necessary to contract with experts in this field. This augmentation would result in an estimated \$11 million to \$14 million General Fund revenue increase (\$138 million to \$184 million total through 2008-09), over-and-above what the FTB is estimated to collect without these expert consultants.

Staff Comment. According to the Finance Letter, the "investment" of \$400,000 in tax shelter experts will yield a return of between 27.5 and 35 times the initial cost (\$11 million to \$14 million). Given the Administration's past practice of submitting proposals that have an expected cost-benefit ratio of as little as 1:5, a larger investment in ATS consultant services may be prudent.

Staff Recommendation. Hold open and request the FTB report to the **Subcommittee** on the extent to which increased investment in tax shelter experts and other means to identify abusive tax shelters will curb ATS activity and generate General Fund revenues.

8860 Department of Finance

The Department of Finance serves as the Governor's chief fiscal policy advisor. The objectives of the Department of Finance are to (1) prepare, present, and support the annual financial plan for the state, (2) assure responsible and responsive state resource allocation within resources available, (3) foster efficient and effective state structure, processes, programs and performance, and (4) establish integrity in state fiscal databases and systems.

| | 2002-03 | 2003-04 | CHANGE FROM 2002-03 | | 2004-05 | CHANGE FROM 2003-04 | |
|------------------|----------|----------|------------------------|------|----------|------------------------|-------|
| Total Budget | \$40,776 | \$44,111 | \$3,335 | 8.2% | \$43,336 | -\$775 | -1.8% |
| Personnel Years* | 421.2 | 430.6 | 9.4 | 2.2% | 409.7 | 20.9 | -4.9% |

(Dollars in 000s)

*Positions adjusted for salary savings and other adjustments

Issues Proposed for Consent

The following Budget Change Proposals have been submitted by the Administration.

ISSUE #1. Technology Oversight and Security Unit

Administration Proposal. The Department of Finance requests \$2 million in continued funding and 20.3 positions for the information technology oversight and security programs within the Technology Oversight and Security Unit (TOSU). TOSU was established within the Department of Finance as the replacement for the Department of Information Technology. Ongoing funding is needed to continue existing TOSU security and oversight functions.

Staff Comment. The Department of Finance's TOSU unit oversees \$7 billion in IT projects for the state. Without continued funding for these positions, the state will lose an important asset in identifying misuse of state funds on IT programs and oversight for IT risk management. The LAO has raised no concerns with this BCP.

Staff Recommendation. Approve as budgeted the Technology Oversight and Security BCP.

VOTE:

ISSUE #2. Capital Outlay Project Tracking System (COPTS) – Reimbursed Position.

Administration Proposal. The Department of Finance requests one full time permanent Staff Programmer Analyst position in the Information Services Unit to support the department's COPTS. The position will be reimbursed from the Public Works Board, the principal beneficiary of the COPTS.

Staff Comment.

In 2004-05 the state will spend approximately \$1.6 billion in capital outlay expenditures. The implementation of the COPTS will be helpful in managing this immense investment in capital outlay projects by improving the budgeting and sequencing of new and existing projects. The LAO has raised no concerns with this BCP.

Staff Recommendation. **Approve as budgeted** the Capital Outlay Project Tracking System BCP.

VOTE:

9612 Enhanced Tobacco Settlement Asset-Backed Bonds

Chapter 225, Statutes of 2003, requires the Department of Finance to place an item in the budget that would authorize the Director of Finance to allocate from the General Fund should tobacco revenues be below the level required to pay the debt service. This enhancement was to provide assurance to bond purchasers that there will be sufficient funding to pay further debt service. In September 2003, enhanced tobacco bonds were sold at favorable interest rates that resulted in net proceeds to the General Fund of \$2.264 billion.

Administration's Proposal. In accordance with Chapter 225, Statutes of 2003, this item appropriates \$1000 to serve as a backstop should tobacco revenues fall short of making debt service payments on the tobacco bonds. While this authority exists, it is not anticipated that the General Fund will be required to make any payments.

Staff Comments. While statutory authority has been provided to allocate up to \$200 million General Fund, it is not expected to be utilized and the item contains only a \$1000 "placeholder" appropriation. This item is the state's commitment to the bondholders should tobacco revenues fall short of making debt service payments on the tobacco bonds.

Staff Recommendation. **Approve as budgeted** the Enhanced Tobacco Settlement Asset-Backed Bonds budget item.